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In the

Supreme Court of the United States

JANUARY TERM 1967

No. 1127

SOUTHERN BROKERAGE COMPANY,
Petitioner,

v.

DAVID CANNARSA,
Respondent,

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF TEXAS AND THE COURT OF CIVIL APPEALS FOR THE SIXTH SUPREME JUDICIAL DISTRICT OF TEXAS

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Petitioner prays that a writ of certiorari issue to review the judgment of the Supreme Court of the State of Texas, and the Court of Civil Appeals for the Sixth Supreme Judicial District of Texas, and the 134th Judicial District Court of Dallas County, Texas.

OPINIONS BELOW

The opinion of the Supreme Court of the State of Texas is unreported. Its order refusing the application for writ of error to the Court of Civil Appeals for the Sixth Supreme Judicial District of Texas at Texarkana, Texas is set forth in Appendix B at page 11. Its order refusing Motion for Rehearing is set out at page 11 of Appendix B. The Court of Civil Appeals opinion is reported in 405 S.W. 2d 457. It is set forth in Appendix B hereto beginning at page 1.

JURISDICTION

The Petitioner's Application for Writ of Error to the Court of Civil Appeals for the Sixth Supreme Judicial District was refused by the Supreme Court of the State of Texas on October 12, 1966 (R. 11). The Supreme Court of the State of Texas denied Petitioner's Motion for Rehearing on November 9, 1966 (R. 11). An extension of time within which to file this Petition for Writ of Certiorari until and including March 7, 1967 was granted by this Court. The jurisdiction of this Court is invoked under Section 1257(3) of Title 28, U.S.C.A.

QUESTION PRESENTED

The question presented is whether or not the Courts below have erroneously required the performance of a contract, the performance of which would violate an injunction of a United States District Court, the Securities Act of 1934, and the Rules and Regulations of the Securities and Exchange Commission.

STATUTES INVOLVED

The statutory provisions involved are Section 78j of the Securities Exchange Act of 1934 (15 U.S.C.A. 78j), Section 78i of the Securities Exchange Act of 1934 (15 U.S.C.A. 78i), Section 10(b)-5 of the Securities Exchange Act of 1934 (17 C.F.R. §240:10b-5), and Section 29(b) of the Securities Exchange Act of 1934 (15 U.S.C.A. 78cc). They are printed in Appendix A, infra, pp. 1, 2, and 3.

STATEMENT OF THE CASE

This is a suit for breach of contract for the purchase of stock of Jerome Richards & Co. Petitioner refused to complete the purchase from Respondent after it was learned that the Securities Exchange Commission was investigating the affairs of one Kamen & Company in its dealings with said stock (S.F. 52, 53, 68, 69, 158, 159). Kamen & Company had instructed the Respondent to purchase 700 shares of Jerome Richards & Co., Inc. stock at one price from one firm (Frederick Cirlin & Associates) and sell it to Petitioner at a slightly higher price, simultaneously instructing Petitioner to sell it to a third party at a still higher price (S.F. 19, 82, 83, 100, 116). After Petitioner and Respondent discovered that the Commission was investigating Kamen & Company in its dealings with said stock and that the party to whom the Petitioner was to sell the stock was nonexistent, it refused to honor its confirmation to purchase the stock (S.F. 52, 53, 55, 57, 73, 74, 116, 121). A subsequent United States District Court action was immediately instituted by the Securities Exchange Commission naming

Kamen & Company as one of the defendants and citing certain manipulative devices with respect to its trading of the stock in question. A subsequent injunction was issued to the knowledge of both Petitioner and Respondent (S.F. 67, 68). The Court of Civil Appeals opinion accurately states the sequence of events with respect to the trading of this stock (Appendix B; pp. 2-5). Subsequent to Petitioner's Application for Writ of Error filed in the Supreme Court of the State of Texas, disciplinary action was taken against Kamen & Company and Frederick Cirlin and Associates (Securities Exchange Act Release No. 7965). This fact was not in evidence at the time of the trial of this cause, but was brought to the attention of the Supreme Court of the State of Texas, in its Motion for Rehearing. (p. 2).

REASONS FOR GRANTING THE WRIT

1. The decision of the court below effects the enforcement of an illegal transaction in violation of an injunction issued by a United States District Court, thus putting Petitioner in jeopardy of punishment of contempt of court and furthering a fraudulent scheme condemned by Federal authorities who had exclusive jurisdiction.

2. The decision of the court below discounts the uncontradicted evidence that such a transaction was fraudulent or was for the purpose of creating a false and misleading appearance of active trading or a false and misleading appearance with respect to the market for the stock in question or a component of a larger scheme for that purpose.

The evidence is undisputed from the opinion of the Court of Civil Appeals and the testimony of the witnesses in the course of their testimony in trial court, that the Securities Exchange Commission had investigated the trading in Jerome Richards & Co., Inc. stock prior to the consummation of the transaction herein by Petitioner and Respondent (S.F. 68, 69, 158, 159). It is also undisputed that the Securities Exchange Commission subsequently obtained an injunction in a United States District Court enjoining Kamen & Company and others from dealing in the stock (C.C.A. Opinion, p. 2, S.F. 67, 68) (Appendix B, p. 4). While it is not apparent from the record that Jerome Richards & Co. Inc. stock is a registered stock or a listed stock, the Securities Exchange Act of 1934 declares that certain manipulative practices are unlawful for the purpose of creating a false or misleading appearance of active trading in any security registered on a national exchange or a false or misleading appearance with respect to the market for any such security. (Appendix A at page 1). The Securities Exchange Act of 1934 (15 U.S.C.A. 78j) further declares that certain manipulative practices are unlawful with respect to securities, whether they be registered or not. (Appendix A hereto at pages 1-2) The Commission's Rule 10b-5 (17 C.F.R. 240:10-b) was intended to implement Section 78j of the Securities Act of 1934. (Appendix A at page 2).

In the case of U. S. v. Morgan, D.C. N.Y. 1953, 118 F. Supp. 621, the Court stated that that section of the Securities Exchange Act of 1934 relating to the purchase and/or sale of a registered or listed security in order to stabilize

the price was intended to apply in the same manner to an unregistered security as dealt with in 15 U.S.C.A. 78j of the Securities Exchange Act of 1934. It should be noted that so-called "matched orders" provision is more fully described in Section 78i than in Section 78j. It seems clear, however, from the Morgan case that the same standard would apply to both registered and unregistered securities.

The opinion of the Texas Court of Civil Appeals states: "This activity indicates Kamen & Company had an active interest in the distribution of Jerome Richard & Co. Inc. stock but in the absence of evidence Kamen & Company intended and purposed to manipulate the market in a prohibited way, this proof of that brokerage house's enterprise, standing alone or in connection with any other facts developed in the record, does not lead to the single conclusion that Kamen & Company and the brokers it used singly or collectively engaged in a prohibited or fraudulent market activity". (Appendix B, page 9). The Court of Civil Appeals either ignored or failed to consider the undisputed evidence with regard to the investigation of Kamen & Company by the Securities Exchange Commission, the District Court action, its subsequent injunction, and the fact that Petitioner's buyer was fictitious or nonexistent.

The Securities Exchange Act of 1934, Section 29(b) provides a civil remedy for the parties to a contract without regard to any injunctive relief which might be sought by the Commission (Appendix A, pages 2-3). The very practice which was being directed by Kamen & Company with Petitioner and Respondent conforms exactly with those manipu-

lative practices proscribed in Section 78i, 78j and Commission Rule 10b-5 of the Securities Act of 1934. The action in the Federal District Court corroborates the fraudulent nature of the activity and it is not significant that Petitioner and Respondent were not parties to the Federal District Court action. Such activity is unlawful regardless of the intent of the parties at its inception.

It seems clear that the language of Section 29(b) of the Securities Act of 1934 provides a sufficient ground for rescission, but also for money damages. (Geismar v. Bond & Goodwin, Inc., 40 F. Supp. 876). The cited case concerned the sufficiency of the complaint to bring a cause of action within the provisions of the Securities Exchange Act of 1934 and therefore subject to Section 29(b) declaring such contracts void. While a violation of a different section of the Act is alleged than in the instant case, it is unequivocably stated that Section 29(b) allows rescission or other appropriate action. This Petitioner therefore is entitled to relief either by way of defense or by way of a declaratory judgment that the contract is void.

The law of Texas as to the enforcement of an illegal contract is well stated by the Supreme Court of Texas in *Morrison v. City of Fort Worth (1941)* 155 S.W. 2d 908, 909, where the Court wrote:

"We think further that it is the settled law in this State that our courts will neither aid in the enforcement of an illegal executory contract, nor relieve from an illegal contract a party who has executed it. (Authorities). These

authorities could be multiplied several times, but we think they are sufficient to establish the correctness of the rule we have announced.". In Ferguson v. Mounts, 281 S.W. 616, 621, the rule is stated thus:

"When the performance of a contract otherwise legal will involve the violation of a statute or positive rule of law, it is not enforceable and cannot be ratified, nor its terms made binding by ratification, waiver or otherwise. *Rue v. Missouri Pacific Ry. Co.*, 88 S.W. 533, 74 Tex. 474, *Raywood Rice, C & M Co. v. Erp*, 146 S.W. 155, 105 Tex. 161, *Chimene v. Pennington*, 79 S.W. 63, 34 Tex. Civ. App. 424."

In Houston Fire & Casualty Insurance Co. v. Pritchard & Abbott, 283 S.W. 2d 728, the Court wrote:

"An action to rescind is not the only legal means of being relieved of the obligation of a contract made under a mistake of fact; relief may also be obtained by defending against an asserted liabilty on the contract."

The United States Circuit Court of Appeals in Chas. Hughes & Co. v. Securities Exchange Commission (139 Fed. 2d 434, Certiorari Denied, 321 U.S. 786) wrote:

"The law of fraud knows no difference between express representation on the one hand and implied misrepresentation or concealment on the other * * *. The best element of business has long since decided that honesty should govern competitive enterprises, and that the rule of caveat emptor should not be relied upon to reward fraud and deception. Federal Trade Commission v. Standard Education Society, 302 U.S. 112, 116 * * *. Indeed it is the purpose of

all legislation for prevention of fraud in the sale of securities to preclude the sale of "securities which are in fact worthless, or worth substantially less than the asking price."

In addition, the Securities Exchange Act of 1934, Section 29 provides that all contracts entered into in violation of any provisions of that chapter or of any rule or regulation thereunder shall be void as regards the right of any person who engaged in the performance of any such contract and as regards the rights of any party, even though not a party to such contract, who shall have acquired any right acquired thereunder with actual knowledge of such facts. For Petitioner to have consummated the purchase of the stock in the light of knowledge as to its illegality would have fostered the scheme and manipulative devices which the law has condemned. For the courts below to have compelled performance under the facts was a substantial deprivation of petitioner's property without due process of law.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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